

1 **GOVERNMENT OF THE DISTRICT OF COLUMBIA**
2 **DEPARTMENT OF INSURANCE AND SECURITIES REGULATION**

3 **IN THE MATTER OF**)

4 **U.S. BANCORP PIPER JAFFRAY INC.**)

5 **800 NICOLLET MALL**)

6 **SUITE 800**)

7 **MINNEAPOLIS, MN 55402,**)

8 **RESPONDENT.**)

ADMINISTRATIVE CONSENT ORDER
 SEC. CO 03-06

9 **ADMINISTRATIVE CONSENT ORDER**

10 WHEREAS, U.S. Bancorp Piper Jaffray Inc. (hereinafter "USBPJ") is a broker-dealer
11 registered in the District of Columbia; and

12 WHEREAS, coordinated investigations into USBPJ's activities in connection with certain
13 of its equity research and investment banking practices during the period of approximately 1999
14 through 2001 have been conducted by a multi-state task force and a joint task force of the U.S.
15 Securities and Exchange Commission, the New York Stock Exchange, and the National
16 Association of Securities Dealers (collectively, the "regulators"); and

17 WHEREAS, USBPJ has cooperated with regulators conducting the investigations by
18 responding to inquiries, providing documentary evidence and other materials, and providing
19 regulators with access to facts relating to the investigations; and

20 WHEREAS, USBPJ has advised regulators of its agreement to resolve the investigations
21 relating to its equity research and investment banking practices; and

22 WHEREAS, USBPJ agrees to implement certain changes with respect to its equity research
23 and investment banking practices, and to make certain payments; and

24 WHEREAS, USBPJ voluntarily elects to permanently waive any right to a hearing on this
25 matter and judicial review of this Administrative Consent Order (the "Order") under D.C. Official
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1 Code § 31-5606.02 (b) (2001 ed.);

2 NOW, THEREFORE, the Commissioner of the Department of Insurance and Securities
3 Regulation, as administrator of the Securities Act of 2000, D.C. Official Code § 31-5601.01 *et seq.*
4 (2001 Ed.) hereby enters this Order:

5 I.

6 FINDINGS OF FACT

7 A. Background and Jurisdiction

- 8 1. USBPJ is a broker-dealer with its principal place of business in Minneapolis, Minnesota. The
9 firm engages in a full-service securities business, including retail and institutional sales,
10 investment banking services, trading, and research.
- 11 2. USBPJ is a broker-dealer registered in the District of Columbia.
- 12 3. This action concerns the years 1999, 2000, and 2001 (the "relevant period"). During that
13 time, USBPJ engaged in both research and investment banking ("IB") activities.
- 14 4. At various times during the relevant period, USBPJ placed undue emphasis on using its
15 research analysts to maximize opportunities to obtain investment-banking revenues from
16 companies in the technology, telecommunications, and biotechnology industry sectors. Such
17 emphasis on obtaining investment-banking revenue created conflicts of interest for the
18 research analysts that resulted in the issuance of research reports. USBPJ failed adequately to
19 monitor and supervise the conflicts of interest inherent in seeking investment-banking
20 opportunities from companies covered by USBPJ research analysts. USBPJ's violative
21 conduct, described herein, was caused by a flawed organizational structure, combined with
22 inadequate supervision of the conflicts of interest.
- 23 5. USBPJ grouped its research analysts by industry sector and those analysts worked as a team
24 with the firm's investment bankers, who focused on the same industry sector. The majority of
25 research analysts' compensation was paid in the form of bonuses, which for some analysts
26 was directly tied to revenues from investment banking transactions of companies in their

1 industry sector. In other cases, the analyst's contribution to investment banking revenue, and
2 investment banker input into analysts' evaluations played a significant part in determining the
3 analysts' bonuses. In certain cases, investment bankers commented in reviews that research
4 analysts needed to become lead analysts, a reference to using their professional opinions and
5 reports to assist the firm in obtaining the top role in investment banking transactions. As a
6 result of these influences, certain USBPJ research analysts indirectly were motivated to
7 obtain, retain and increase investment-banking revenue.

- 8 6. In certain instances, USBPJ also provided draft research reports to potential investment
9 banking clients during sales pitches, and this implicit promise of favorable research was an
10 important aspect of USBPJ's attempts to gain the companies' investment banking business.
11 In other instances, after determining to issue research, USBPJ provided company executives
12 with draft reports, including the proposed rating and target price, and solicited comments on
13 the report from those company executives.
- 14 7. USBPJ failed to disclose that it received compensation from the proceeds of underwriting for,
15 among other services, providing research. It also paid proceeds of certain underwritings to
16 other broker dealer firms to issue research on companies whose offerings it underwrote and
17 did not ensure that such payments were disclosed.
- 18 8. Finally, USBPJ engaged in improper behavior by threatening to drop research coverage on a
19 company if USBPJ did not receive a certain role in the company's offering of securities.
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21 **B. USBPJ's Structure and Procedures Encouraged Research Analysts to Contribute to**
22 **Investment Banking Revenue, Thus Creating Conflicts of Interest**

23 **(1). Overview of USBPJ and the Financial Contribution of its Equity Capital Markets**
24 **Division**

- 25 9. USBPJ was founded in 1895.¹ The firm is headquartered in Minneapolis, Minnesota, and has
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¹ U.S. Bancorp acquired USBPJ Inc., as a subsidiary in 1998.

1 approximately 3,100 employees, including approximately 875 financial advisers, more than
2 80 investment bankers, and approximately 70 research analysts. USBPJ has operations in 124
3 offices in 25 states throughout the country.

4 10. During the relevant period, USBPJ's business included retail brokerage, known as Private
5 Advisory Services; fixed income underwriting, sales and trading (known as Fixed Income
6 Capital Markets); and equities investment banking, syndicate, research, and institutional sales
7 and trading (known as Equity Capital Markets or "ECM"). Thus, equity research and
8 investment banking were in the same business line and, ultimately, reported to the same
9 individual.

10 11. In 1998, USBPJ generated equity investment banking revenue of approximately \$79,500,000.
11 That increased by 100 percent to approximately \$159,000,000 in 1999. In 2000, revenue
12 from equity investment banking grew to approximately \$269,200,000, a 69 percent increase
13 over 1999. In 2001, USBPJ's revenue from equity investment banking was approximately
14 \$153,000,000. From 1999 through 2001, revenue from equity investment banking
15 represented a significant portion of the firm's revenue, accounting for between 19 – 26
16 percent of the firm's total revenue.

17 **(2). USBPJ Aligned Research Analysts With the Firm's Investment Bankers**

18 **(a). USBPJ Developed and Implemented Specific Plans To Have**
19 **Research Analysts Work With Investment Bankers in an Effort to**
20 **Obtain Investment Banking Business**

21 12. During the relevant period, many companies, particularly those in the technology area, issued
22 stock through public offerings, and there was intense competition among investment banking
23 firms to obtain this business. In order to maximize its chances to participate in these
24 offerings, USBPJ made a concerted effort to include its research analysts in its solicitation of
25 this business. This effort included developing and implementing specific marketing plans,
26 which provided for research analyst involvement in the investment banking process.

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(i). Move to the Left Strategy

13. In May 2000, USBPJ's ECM Operating Committee amended its procedures and strategies in a specific effort to gain lead manager status in more offerings. The Lead Manager is the firm typically listed on the left side of the offering prospectus. Thus, USBPJ implemented a plan referred to as the "Move to the Left Strategy." The ECM Operating Committee noted its strong commitment to a "multi-pronged strategy" to obtain lead-manager status on offerings. In instructions to ECM employees, the ECM Operating Committee stated that the firm "must begin to wage a war in earnest for lead-manager status." That plan instituted a "line in the sand" policy: The firm would not accept a syndicate position in any deal unless the firm was placed in the major bracket for the underwriting.
14. The Research Department played an important role in the firm's Move to the Left Strategy. Specifically, to develop a "lead manager mentality," the firm developed a "lead manager Red Zone training program." That program called for the senior bankers, senior research analysts, and Capital Markets personnel to "go through this special training seminar [focused] on pitching for the lead on public equity transactions."

(ii). Lead Manager Protocol

15. In August 2000, the head of ECM's syndicate department prepared another specific effort to gain additional lead managed offerings. In setting out his new "Lead Manager Protocol" to all ECM employees, the head of the syndicate department stressed that the "formal protocol of responsibilities ... will allow all of us—Investment Banking, Research, Sales, Trading and Capital Markets—to share responsibility for the success of each and every lead-managed offering."
16. The Lead Manager Protocol, issued in August 2000, called for:

- 1 • the lead banker and lead research analyst to make a presentation to the firm's Pre-
2 Commitment Committee before any company would be considered for an underwriting;
3 • the research analyst to participate in a "get-to-know-you" session with prospective
4 investment banking clients as part of a "Day at Piper" session;
5 • the lead banker and senior analyst to re-present the prospective company client to the
6 Commitment Committee. The lead banker and "senior analyst must demonstrate continued
7 due diligence effort and must provide renewed commitment to the transaction";
8 • research and sales to "set up a roadshow schedule to ensure a targeted and efficient
9 roadshow.... [and] focus on ascertaining the right accounts to see and why these are the
10 right accounts;"
11 • senior analysts to "provide aggressive pre-meeting preparation and post-meeting follow-up
12 to each 1-on-1 appointment;"
13 • senior analysts to be "available during critical parts of roadshow and pricing"; and
14 • the senior analyst to "coordinate with Capital Markets to sort out the aftermarket intentions
15 of each account."
16 17. The Lead Manager Protocol described a primary function of a research analyst in
17 communicating regarding the progress of the transaction once the firm had obtained a lead
18 management role in an IPO when it stated: "Senior analyst will coordinate with Capital
19 Markets to communicate a consistent message regarding the progress of the transaction,
20 acting as a supporter of Capital Markets' message and not as an independent filter The
21 goal of the [s]enior analyst is to reinforce reasonable and exceedable expectations."

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23 **(b). Research Analysts "Pitched" for Investment Banking Deals and**
24 **Advocated for the Issuer at Roadshows**

- 25 18. USBPJ's procedures allowed for the close alignment of research analysts with investment
26 bankers in the same industry sector. ECM marketed to potential clients its research coverage,

1 market making and institutional sales as part of the firm's efforts to obtain investment
2 banking business. USBPJ used the slogan, "One Team, One Business" in its marketing
3 materials with prospective investment banking clients. Internally, the company had
4 "transaction teams" that included investment bankers and research analysts.

- 5 19. The emphasis on securing investment banking business through pitches and then selling the
6 securities through roadshows gave rise to conflicts of interest for the research analysts. In
7 some instances, the research analyst became a prime contact person for the company with
8 respect to soliciting investment-banking business. For example, on May 10, 1999, a research
9 analyst wrote to an officer of E-Machines, a potential investment-banking client: "This is my
10 final appeal to be a part of the underwriting team. This is your deal and you control the
11 strings. All we are looking for is ten percent of the economics to participate in the
12 underwriting. This itself should be indicative of my sincere interest in your story ... In the
13 final analysis, it is less important to have bulge bracket firm as a hood ornament than it is to
14 have a quality analyst who will provide you with the support and coverage your company
15 needs."

16 **(c). Research Analysts' Participation in Pitch Meetings Was Important in**
17 **Obtaining Investment Banking Mandates**

- 18 20. Before USBPJ made its "pitches" to an issuer for investment banking business, the investment
19 banker, teamed with a research analyst for the appropriate sector, would make a presentation
20 to USBPJ's Pre-Commitment Committee. This presentation included a recommendation and
21 analysis detailing why the firm should pursue an investment banking relationship with the
22 issuer. After USBPJ determined to compete for a company's investment banking business,
23 particularly in the case of an initial public offering ("IPO"), the research analyst's role was
24 influential in obtaining that business.
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1 21. One aspect of a research analyst's function was to play a key role in the process to "pitch"
2 USBPJ to the prospective client. In certain instances, a research analyst's role at a pitch
3 meeting with an issuer was to assist investment banking personnel in convincing the issuer
4 that USBPJ should be chosen as the lead managing underwriter for the offering. A research
5 analyst's presence suggested that the Research Department would work hand-in-hand with the
6 investment bankers to provide service and support for the issuer. Research analysts routinely
7 appeared with investment bankers at pitch meetings designed to help sell USBPJ to the
8 potential client and provided information relating to their research in pitchbooks given to
9 prospective client companies.

10 **(d). In Certain Instances, Pitchbooks Provided to Potential Investment**
11 **Banking Clients Contained Mock Research Reports Impliedly Promising**
12 **Favorable Research**

13 22. When investment bankers and research analysts presented "pitches" to prospective investment
14 banking clients, USBPJ typically gave the prospective client a pitchbook explaining the
15 proposed services to be provided by the firm. These pitchbooks detailed, in a most favorable
16 manner, why USBPJ should be selected to underwrite the offering. In addition to providing
17 information about how USBPJ would conduct the underwriting, the pitchbooks routinely
18 included a roadmap of the amount and type of research coverage that USBPJ would provide
19 to support the company if it obtained the investment banking business. In certain instances,
20 USBPJ included a "mock" research report for the companies, containing a valuation analysis
21 and "mock" rating such as "buy," impliedly promising to the issuer that the research analyst
22 would issue a favorable research report if it selected USBPJ for the investment banking
23 business. In some instances, USBPJ's mock research reports also included a favorable
24 "mock" target price for the issuer's stock.

25 23. For example, in August 2000, USBPJ made a pitch to be the lead underwriter for an offering
26 by TheraSense, a medical technology issuer. In preparing for the pitch, a research analyst

1 prepared a mock research report about the issuer and presented that mock report at the pitch
2 meeting. The mock research report noted in several places a proposed rating of "Strong Buy."
3 The mock report contained very positive news about the company, claiming that its initial
4 sales of the product were "nothing short of breathtaking." In part, as a result of that pitch, the
5 company awarded USBPJ the role of lead managing underwriter, which generated
6 underwriting fees of \$3,785,512 for the firm when the offering went effective in October
7 2001. USBPJ initiated coverage of the issuer with a "Strong Buy" recommendation shortly
8 after the offering went effective.

- 9 24. Finally, after USBPJ was awarded an investment-banking mandate, another key function for a
10 research analyst was to provide meaningful support to the firm's institutional investor clients
11 to ensure that an underwriting was successful. Investment bankers, research analysts and
12 company representatives generally traveled to the offices of institutional investor clients, to
13 meet with them and describe the offering and determine their interest in purchasing the stock.
14 At times, research analysts attended and provided significant assistance at these "roadshow"
15 meetings.

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17 **(3). USBPJ Tied Research Analysts' Compensation to Investment Banking Revenue**

- 18 25. During the relevant period, USBPJ compensated research analysts, in part, based on the
19 amount of investment banking revenue generated within their respective industry sector. This
20 practice created a conflict of interest for research analysts, since analysts were compensated,
21 in part, on issuing objective research and on the firm's success in obtaining investment-
22 banking business.
- 23 26. Specifically, USBPJ paid certain analysts a percentage of investment banking revenue and
24 institutional commissions generated by companies in their industry sector. The firm entered
25 into written agreements with at least 16 research analysts to pay them a defined percentage of
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1 the revenue generated by the companies they covered. This included revenue from net
2 underwriting profits, institutional sales commissions, trading commissions, equity and debt
3 management fees, mergers and acquisition advisory fees, equity and debt private placement
4 fees, research checks, and syndicate trading profits. The defined percentage set forth in these
5 written agreements ranged from a guaranteed 7 to 15 percent of the revenues generated by the
6 companies in their industry sector.

7 27. Compensation for other research analysts was comprised of base salary plus a bonus.
8 Investment banking revenue was a significant factor in determining the bonus. The bonus
9 was based, in part, on investment banking revenue received from companies in the specific
10 industry sector that each analyst covered, and the level of contribution the research analyst
11 made in the effort to obtain the investment banking business. The bonus usually formed the
12 majority of a research analyst's total compensation. In 1999 and 2000, for example, more
13 than 85 percent of a typical research analysts' compensation came from the bonus, while in
14 2001 approximately 77 percent of a typical research analyst's compensation was in the form
15 of a bonus. During that time, research analysts' salaries generally ranged from \$60,000 to
16 \$250,000, while the discretionary bonuses ranged from \$75,000 to \$4,000,000.

17 28. In determining the amount of discretionary bonuses, supervisors in the research department
18 considered, among other things, a research analyst's contributions to the firm's success in
19 obtaining investment-banking revenues. Performance evaluations of the research analysts
20 demonstrate this consideration. Research analysts received periodic reports detailing the
21 year-to-date revenues generated by their covered companies. At times, senior investment
22 bankers provided these reports to the research analysts, as well as to investment banking
23 employees, and listed the projected investment banking revenue goals for the covered
24 companies. One supervisor noted in a performance evaluation that a certain analyst should
25 work on becoming a "lead managing analyst." That expression was a reference to the lead
26 managing underwriter position that USBPJ sought in offerings because it resulted in the

1 greatest amount of control and revenue. Thus, the supervisor's expression acknowledged the
2 role that an analyst could play at USBPJ in obtaining investment-banking business. For
3 example, one senior analyst received a salary of \$160,000 and a bonus of over \$3.8 million.
4 In another example, an analyst received a salary of \$130,000 and a bonus of over \$3 million.
5 In both of these instances, the bonus determination included consideration of investment
6 banking and trading revenues for companies in the industry sector covered by the analyst.
7 29. The fact that research analysts contributed to the firm's efforts to obtain investment-banking
8 revenue is also evident from the personal goals set by certain research analysts. Some
9 analysts, in setting forth their goals, stated specific investment banking revenue goals and
10 listed the ongoing support of investment banking and sales as important to their continued
11 success.

12 **(4). Investment Bankers Evaluated Research Analysts' Performance and Influenced**
13 **Their Bonus Compensation**

14 30. In 2000 and 2001, investment bankers who worked on investment banking business with
15 research analysts participated in the annual performance evaluations of those research
16 analysts. Specifically, in certain instances, investment bankers completed and provided to the
17 Director of Research a "Banker Peer Review" on certain research analysts. Investment
18 bankers evaluated research analysts using specific criteria, including:

- 19 • "proactively generates and shares valuable M&A/strategic ideas;"
- 20 • "prepares for pitches and contributes to preparation of pitchbook;"
- 21 • "effective in pitches; [and] takes the aftermarket commitment seriously."

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23 31. Thus, investment bankers provided significant input in the performance evaluation of research
24 analysts which, in turn, influenced the bonus compensation of those research analysts. For
25 example, an investment banker noted in his banker peer review that a particular analyst:
26 "needs to be proactive in pursuing fee-generating companies for his coverage list. He is very

1 focused on big cap names that do not pay.”

2 32. This review process indicated to research analysts that, in part, their role was to assist the
3 investment bankers and the firm’s investment banking clients.

4 **(5). USBPJ Lacked Procedures and Did Not Adequately Monitor Research Analysts’**
5 **Sharing of Draft Research Reports With Issuers**

6 33. In certain cases, prior to the dissemination of research reports, USBPJ research analysts
7 provided copies of their draft reports to an issuer’s executives, and solicited comments and
8 suggestions for such reports. Providing draft research reports to an issuer’s executives could
9 potentially compromise a research analysts’ independence in that the investment banking
10 clients may pressure the analyst to make inappropriate changes to the draft report.

11 34. Certain draft research reports provided to an issuer included not only the factual portions of a
12 draft report, but also the analyst’s valuation, rating and suggested target price. In some cases,
13 company executives were given electronic copies of the research report, and returned to the
14 firm a “red-lined” version of the report with their comments and edits. For example, on
15 September 27, 2001, a USBPJ research analyst sent a representative of Genta, Inc. an e-mail
16 containing a draft report with a rating. This e-mail stated, “ Hope you are doing better. Here
17 is a draft of our initiation note. Please review it and send me any comments you may have.
18 Thanks...” On October 2, 2001, Genta responded to the e-mail with extensive comments on
19 the note.

20 35. In other instances, USBPJ investment bankers suggested to issuer clients that research reports
21 initiating coverage would be subject to approval by the issuer. For example, on January 11,
22 2001, an investment banker wrote to numerous executives at Metromedia Fiber Network, Inc.
23 (“Metromedia”) thanking them for their meeting with a USBPJ senior research analyst. The
24 banker wrote, “[The analyst] has decided to initiate coverage with a Strong Buy, our firm’s
25 highest recommendation...his research associate...will be calling you later today to request
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1 help in finalizing the report. *Nothing will be published without your prior approval.*"
2 (Emphasis added). On January 26, 2001, USBPJ initiated coverage of Metromedia with a
3 "strong buy" and a \$27 price target.

4 36. On November 22, 2000, a USBPJ senior investment banker wrote to executives of Qwest
5 thanking them for an in-person meeting. The banker wrote: "We expect to initiate research
6 coverage within the next few weeks and will submit a draft of such report for your review and
7 approval prior to publication."

8 37. Notwithstanding the potential that research analysts could be subjected to pressure by issuers,
9 USBPJ failed to have adequate procedures or controls to monitor such communications.

10 **(6). USBPJ Lacked Procedures And Controls Sufficient To Monitor The Influence of**
11 **Investment Banking on Research Analysts**

12 38. In view of the interaction between research analysts and investment banking described above,
13 USBPJ lacked adequate systems or procedures to supervise the influence that investment-
14 banking opportunities had on research personnel. For example, on January 17, 2001, a
15 USBPJ senior research analyst wrote an e-mail to a junior analyst seeking input as to whether
16 he should maintain a "buy" rating on Natural Microsystems, Inc. ("NMSS"). USBPJ had
17 downgraded NMSS from "strong buy" in December 2000 based on the company's
18 announcement that it would likely miss its earnings projections for the year. Upon the
19 company's announcement in January 2001 that it had, in fact, not met its projections for 2000,
20 the senior analyst again evaluated the company's rating. In response to the senior analyst's
21 request for input, the junior analyst responded that, in his opinion, the company should stay a
22 "buy" "taking into consideration banking relationship," but that absent such considerations he
23 would rate the stock a neutral.

24 39. On January 18, 2001, USBPJ issued a research report that maintained the previously lowered
25 "buy" rating.² The report included a lower price target than that published previously,
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² USBPJ widely distributed its research through public services such as Thompson Financial's First Call and on its

cautionary statements about NMSS's short-term prospects and a predicted "struggle" for the company's shares during the first half of 2001. In the same research report, USBPJ lowered its revenue estimates by almost one half and reduced the earnings per share to show a loss in fiscal year 2001. At that time, USBPJ defined a "buy" rating as: "Expect positive price appreciation over next 12 months; Solid long term company fundamentals; attractive long-term valuation, though shares may be extended based on near-term parameters." USBPJ subsequently lowered its rating to "neutral" on April 12, 2001.

40. Moreover, USBPJ rarely issued a sell rating. During most of the review period, USBPJ had a four point rating scale: strong buy, buy, neutral, and sell. More than 80 percent of the research reports issued contained either “buy” or “strong buy” recommendations, with less than 20 percent of the companies, on average, rated as a “neutral.” Throughout the review period, USBPJ gave less than one percent of companies a “sell” recommendation. In certain cases, the firm would discontinue coverage, usually without explanation, rather than drop a company to a sell rating. In those cases, therefore, USBPJ had only a three point rating system.

C. USBPJ Issued Research on Two Companies That Lacked a Reasonable Basis Or Was Imbalanced

41. As to two companies, Esperion Therapeutics, Inc. and Triton Network Systems, USBPJ issued research reports that lacked a reasonable basis or were imbalanced.

(1). Esperion Therapeutics, Inc.

42. In August 2000, USBPJ served as co-manager for the IPO of Esperion Therapeutics, Inc. (“Esperion”) and consequently initiated research coverage of Esperion on September 5, 2000 with a “buy” rating. On January 9, 2002, a USBPJ senior research analyst stated in an e-mail

website www.gotoanalyst.com.

1 to a senior investment banker: "ESPR delayed a pipeline product and completely dropped
2 development of a second pipeline product, giving a reason that was nothing short of hokey.
3 So it was bad news all around....Esperion has not met a single milestone that they have laid
4 out since they went public. Everything has slipped. [Esperion's CEO] is a good scientist, an
5 awful CEO."

- 6 43. Notwithstanding these statements, USBPJ's January 2002 industry report "Investing in
7 Biotechnology" and research report on January 24, 2002, both reiterated the existing buy
8 rating (now termed outperform).

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10 **(2). Triton Network Systems**

- 11 44. In July 2000, USBPJ served as co-manager for Triton Network Systems ("Triton")'s IPO. On
12 August 7, 2000, a USBPJ senior research analyst initiated research coverage of Triton with a
13 "buy" rating and a \$45 price target. Soon after the IPO, shares of Triton reached a high of
14 \$47.75, but the value of the stock quickly declined. USBPJ maintained a "buy" rating while
15 the stock price declined to \$1 13/16 over the next eight months.
- 16 45. On March 30, 2001, the analyst issued a "blast" e-mail to institutional clients with cautionary
17 statements about Triton due to the likely loss of a key customer, Advanced Radio Telecom,
18 which was considering a Chapter 11 bankruptcy filing. Other than the "blast" e-mail, USBPJ
19 did not issue a new research report directly on that information at that time. Notwithstanding
20 this negative news, USBPJ maintained a "buy" rating. Another month passed before USBPJ
21 disclosed in a broadly disseminated research report Triton's problems with this customer
22 while downgrading Triton to a neutral on May 1, 2001. After two more months, when Triton
23 was trading below \$1, the research analyst told the head of USBPJ's equity research
24 department, that since the company was in bankruptcy proceedings, "we can drop now if
25 banking says ok." USBPJ discontinued coverage of Triton with a last published rating of
26 neutral.

1 **D. USBPJ Threatened to Drop Research Coverage of Emisphere Technologies, Inc., if it Did**
2 **Not Award USBPJ the Lead Manager Role in an Offering**

3 46. In September 1999, USBPJ attempted to compel Emisphere Technologies, Inc. to select it for
4 investment banking business by informing company executives that it would drop research
5 coverage of the company if it were not selected as the lead manager for an offering of
6 Emisphere's securities. USBPJ's threatening conduct undermined competition for investment
7 banking services.

8 **E. USBPJ Failed to Disclose That it Received Payments From Proceeds of Certain**
9 **Underwritings, In Part, To Publish Research Regarding The Issuer**

10 47. From 1999 through 2001, USBPJ received payments out of the proceeds of certain
11 underwritings to compensate the firm for services that included publishing research on the
12 issuer. These payments were made in the form of "research guarantees" or "research
13 checks." During this period, USBPJ accepted more than \$1.8 million in exchange for, among
14 other services, issuing research reports. Despite having an obligation to do so, the firm failed
15 to disclose in research reports or elsewhere that it received the payments, in part, as
16 compensation for issuing the reports. For example:

17 48. In June 1999, USBPJ received a \$400,000 research check in connection with a \$200 million
18 high yield debt offering in April 1999 for Just for Feet. USBPJ was not a manager on the
19 offering and did not disclose this payment in its ongoing research or elsewhere.

20 49. In July 1999, USBPJ received a \$150,000 check in connection with an offering of common
21 stock by JDS Uniphase Corp. Although USBPJ was not an underwriter in the offering, the
22 firm received the payment, in part, for continued research coverage of the company.

23 50. In March 2001, USBPJ received a \$120,000 research check in connection with an
24 underwriting that went effective in May 2001 for Comverse Technology Inc. USBPJ failed to
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1 disclose in research it published on the company that it had received this compensation, in
2 part, for issuing research regarding the subject company.

3 **F. USBPJ Failed to Ensure Public Disclosure of Payments It Made from the Proceeds of**
4 **Underwritings to Brokerage Firms To Issue Research Coverage Regarding Its Investment**
5 **Banking Clients**

6 51. From 1999 through 2001, at the direction of certain issuer clients, USBPJ paid portions of
7 certain underwriting proceeds to other brokerage firms to initiate or continue research
8 coverage on issuers for which Piper served as lead or co-manager. It knew that these
9 payments were, in part, for research. USBPJ did not take steps to ensure that the brokerage
10 firms paid to initiate or continue coverage of its investment banking clients disclosed that they
11 had been paid to issue such research. Further, USBPJ did not disclose or cause to be
12 disclosed the fact of such payments.

13 52. For example, in 2000, USBPJ paid underwriting proceeds of \$100,000 to another underwriter
14 in conjunction with USBPJ's lead manager position on Onyx Pharmaceuticals' ("Onyx")
15 stock offering. While this underwriter was not invited to participate in Onyx's offering, the
16 payment was made in response to a letter dated September 22, 2000 from the underwriter
17 asking for \$300,000 in "underwriting participation" for continued research and market
18 making. A representative of the underwriter wrote, "From August 31, 1999 until August 15,
19 2000, we were the only firm in print on Onyx Pharmaceuticals and we remain a Strong Buy
20 rating." USBPJ did not ensure that this payment was disclosed to the public in its published
21 research on Onyx.

22 53. In April 2000, USBPJ, acting as lead manager for an offering for Buca, Inc. directed the
23 payment of an aggregate of \$105,000 to three brokerage firms for the issuance of research. In
24 February 2001, while assisting in another investment banking transaction for Buca, Inc.,
25 USBPJ distributed \$225,000 to other firms for their research coverage. USBPJ did not ensure
26 that these payments were disclosed to the public.

1 **G. USBPJ Failed to Adequately Supervise Its Research Analysts and Investment**
2 **Banking Professionals**

- 3 54. During the relevant period, USBPJ's management failed adequately to monitor the
4 activities of the firm's research and investment banking professionals to ensure compliance
5 with state securities laws and regulations. Among other things, this failure to supervise
6 gave rise to and perpetuated the above-described violative conduct.

7 **II.**

8 **CONCLUSIONS OF LAW**

- 9 1. The District of Columbia Department of Insurance and Securities Regulation has
10 jurisdiction over this matter pursuant to the D.C. Official Code § 31-5606.01 (2001 Ed.).
- 11 2. The Commissioner of the Department of Insurance and Securities Regulation finds that
12 Respondent USBPJ engaged in acts and practices that created and/or maintained
13 inappropriate influence by investment banking over research analysts and therefore
14 imposed conflicts of interest on research analysts. USBPJ failed to manage these conflicts
15 in an adequate and appropriate manner.
- 16 3. The Commissioner of the Department of Insurance and Securities Regulation finds that
17 Respondent USBPJ has violated D.C. Official Code § 31-5602.07(a)(9), as described in the
18 Findings of Fact above, by issuing research that contained opinions for which there was no
19 reasonable basis and/or exaggerated or unwarranted claims.
- 20 4. The Commissioner of the Department of Insurance and Securities Regulation finds that
21 Respondent USBPJ inappropriately threatened executives of a potential investment-banking
22 client by stating that they would drop research coverage of the company if the firm was not
23 selected as the lead manager in an investment banking transaction, in violation of D.C.
24 Official Code § 31-5602.07(a)(9).
- 25 5. The Commissioner of the Department of Insurance and Securities Regulation finds that
26 Respondent USBPJ received compensation directly or indirectly, from an issuer,

1 underwriter or dealer, in part, for issuing research reports, without fully disclosing the
2 receipt or the amount of the compensation, in violation of D.C. Official Code § 31-
3 5602.07(a)(9).

4 6. The Commissioner of the Department of Insurance and Securities Regulation finds that
5 Respondent USBPJ, as described in the Findings of Fact above, made payments for
6 research to other broker-dealers not involved in an underwriting transaction, when the firm
7 knew that these payments were made, at least in part, for research coverage, and failed to
8 disclose or cause to be disclosed in offering documents or elsewhere the fact of such
9 payments, in violation of D.C. Official Code § 31-5602.07(a)(9).

10 7. The Commissioner of the Department of Insurance and Securities Regulation finds that
11 Respondent USBPJ failed to establish and enforce written supervisory procedures
12 reasonably designed to ensure that analysts were not unduly influenced by investment
13 banking concerns. Despite knowledge of research analysts' complex responsibilities and
14 conflicts of interest, Respondent USBPJ failed to implement a system to detect and insulate
15 its research analysts from improper influence and pressure by investment banking
16 personnel. To the contrary, Respondent USBPJ's business practices motivated research
17 analysts to issue research that would attract and retain investment-banking business, in
18 violation of D.C. Official Code § 31-5602.07(a) (12).

19 8. The Commissioner of the Department of Insurance and Securities Regulation finds the
20 following relief appropriate and in the public interest.
21

22 III.

23 ORDER

24 On the basis of the Findings of Fact, Conclusions of Law, and Respondent USBPJ's consent
25 to the entry of this Order, for the sole purpose of settling this matter, prior to a hearing and without
26 admitting or denying any of the Findings of Fact or Conclusions of Law.

IT IS HEREBY ORDERED:

1. This Order concludes the investigation by the Department of Insurance and Securities Regulation and any other action that the Department of Insurance and Securities Regulation could commence under the Securities Act of 2000, D.C. Official Code § 31-5601.01 *et seq.* (2001 Ed.) on behalf of the District of Columbia as it relates to Respondent USBPJ, relating to certain research or banking practices at Respondent USBPJ.
2. Respondent USBPJ will CEASE AND DESIST from violating D.C. Official Code § 31-5602.07(a)(9), (12) in connection with the research practices referenced in this Order and will comply with the Securities Act of 2000 and the rules promulgated thereunder in connection with the research practices referenced in this Order, and will comply with the undertakings of Addendum A, incorporated herein by reference.

3. IT IS FURTHER ORDERED that:

As a result of the Findings of Fact and Conclusions of Law contained in this Order, Respondent USBPJ shall pay a total amount of \$32,500,000.00. This total amount shall be paid as specified in the SEC Final Judgment as follows:

- a) \$12,500,000 to the states (50 states, plus the District of Columbia and Puerto Rico) (Respondent USBPJ's offer to the state securities regulators hereinafter shall be called the "state settlement offer"). Upon execution of this Order, Respondent USBPJ shall pay the sum of \$125,000 of this amount to Department of Insurance and Securities Regulation as a civil monetary penalty pursuant to D.C. Official Code § 31-5606.02(b)(4), to be deposited in the District of Columbia's GENERAL FUND, made payable to the 'D.C. Treasurer', pursuant to DC Official Code § 1-204.50. The total amount to be paid by Respondent USBPJ to state securities regulators pursuant to the state settlement offer may be reduced due to the decision of any state securities

1 regulator not to accept the state settlement offer. In the event another state securities
2 regulator determines not to accept Respondent USBPJ's state settlement offer, the
3 total amount of the District of Columbia payment shall not be affected, and shall
4 remain at \$125,000;

5 b) \$12,500,000 as disgorgement of commissions, fees and other monies as specified in
6 the SEC Final Judgment;

7 c) \$7,500,000, to be used for the procurement of independent research, as described in
8 the SEC Final Judgment;

9 Respondent USBPJ agrees that it shall not seek or accept, directly or indirectly,
10 reimbursement or indemnification, including, but not limited to payment made pursuant to
11 any insurance policy, with regard to all penalty amounts that Respondent USBPJ shall pay
12 pursuant to this Order or Section II of the SEC Final Judgment, regardless of whether such
13 penalty amounts or any part thereof are added to the Distribution Fund Account referred to
14 in the SEC Final Judgment or otherwise used for the benefit of investors. Respondent
15 USBPJ further agrees that it shall not claim, assert, or apply for a tax deduction or tax credit
16 with regard to any state, federal or local tax for any penalty amounts that Respondent
17 USBPJ shall pay pursuant to this Order or Section II of the SEC Final Judgment, regardless
18 of whether such penalty amounts or any part thereof are added to the Distribution Fund
19 Account referred to in the SEC Final Judgment or otherwise used for the benefit of
20 investors. Respondent USBPJ understands and acknowledges that these provisions are not
21 intended to imply that the Commissioner of the Department of Insurance and Securities
22 Regulation would agree that any other amounts Respondent USBPJ shall pay pursuant to
23 the SEC Final Judgment may be reimbursed or indemnified (whether pursuant to an
24 insurance policy or otherwise) under applicable law or may be the basis for any tax
25 deduction or tax credit with regard to any state, federal or local tax.
26